

Double digit volume growth in June exudes confidence

- APL's Q1FY21 revenues, EBITDA and APAT came below our estimate due to delayed pick-up in demand compared to our expectation. Nevertheless, double digit volume growth (+14%) in June'20, was a key positive. We believe overall volume de-growth in Domestic Decorative business was 38% in Q1FY21.
- IB posted mixed results as better performance in Africa and ME was offset by Covid led slowdown in Nepal and Bangladesh.
- Considering mixed impact of double digit exit rate for the quarter and lockdowns in few states in July, we believe that growth would normalize in H2FY21E. Consequently, we have maintained our EPS estimates for FY21E and FY22E at Rs 26.4 and Rs 33.5 respectively. We arrive at a TP of Rs 1,840 (55x FY22E EPS). Given rich valuations, we maintain our Reduce rating. Buy on dips.
- We believe that the volume growth in the decorative segment should remain high, especially in rural areas, given better crop production this season. Further, ongoing government investments in rural infrastructure, and house construction in rural areas should partially mitigate overall slowdown. In the long term, we remain optimistic about the paint industry, considering an expected shift from the unorganised to organised sector. APL, being a leader in the category, is likely to benefit the most from the shift.

Results below our estimate

Net Sales declined 42.8% YoY to Rs 29.2bn. Domestic business posted 44.1% net sales de-growth to Rs 24.5bn. Gross margin expanded by 110bps to 44.7%. However, employee/ other expense increased 570/150bps. Consequently, EBITDA margin contracted by 610bps to 16.6%. EBITDA de-grew 58.2% YoY to Rs 4.8bn. APAT declined 66.8% YoY to Rs 2.2bn.

Smaller cities to perform better than metros and Tier 1

After complete washout in April, APL witnessed gradual recovery in May and gained further momentum with double digit volume growth (+14%) in June. Demand in Tier 3 and 4 cities are back to pre Covid levels. Going ahead, we believe that APL would benefit from higher rural contribution (~50%). Rural areas would grow faster compared to urban due to favorable base, relatively lesser Covid impact and increased government spends. Margin expansion would remain a challenge given peaking of GM, lower operating leverage, coupled with expected down trading.

Q1FY21 Result (Rs Mn)

Particulars	Q1FY21	Q1FY20	YoY (%)	Q4FY20	QoQ (%)
Revenue	29,224	51,047	(42.8)	46,356	(37.0)
Total Expense	24,384	39,468	(38.2)	37,760	(35.4)
EBITDA	4,840	11,579	(58.2)	8,596	(43.7)
Depreciation	1,912	1,918	(0.3)	1,945	(1.7)
EBIT	2,928	9,662	(69.7)	6,651	(56.0)
Other Income	471	735	(35.9)	558	(15.6)
Interest	201	267	(24.5)	257	(21.6)
EBT	3,197	10,110	(68.4)	6,953	(54.0)
Tax	862	3,511	(75.5)	2,190	(60.7)
RPAT	2,182	6,554	(66.7)	4,619	(52.8)
APAT	2,182	6,575	(66.8)	4,619	(52.8)
			(bps)		(bps)
Gross Margin (%)	44.7	43.6	109	45.8	(110)
EBITDA Margin (%)	16.6	22.7	(612)	18.5	(198)
NPM (%)	7.5	12.8	(538)	10.0	(250)
Tax Rate (%)	26.9	34.7	(778)	31.5	(455)
EBIT Margin (%)	10.0	18.9	(891)	14.3	(433)

CMP	Rs 1,712
Target / Upside	Rs 1,840 / 7%
BSE Sensex	38,154
NSE Nifty	11,216

Scrip Details

Equity / FV	Rs 959mn / Rs 1
Market Cap	Rs 1,642bn
	USD 22bn
52-week High/Low	Rs 1,917/Rs 1,431
Avg. Volume (no)	2,827,360
NSE Symbol	ASIANPAINT
Bloomberg Code	APNT IN

Shareholding Pattern Jun'20(%)

Promoters	52.8
MF/Banks/FIs	9.2
FII's	17.2
Public / Others	20.8

Valuation (x)

	FY20A	FY21E	FY22E
P/E	60.6	64.7	51.2
EV/EBITDA	39.2	41.1	33.3
ROE (%)	27.6	23.8	27.1
RoACE (%)	23.1	20.2	23.3

Estimates (Rs mn)

	FY20A	FY21E	FY22E
Revenue	202,112	199,931	233,892
EBITDA	41,619	39,365	48,276
PAT	27,101	25,368	32,095
EPS (Rs.)	28.3	26.4	33.5

VP Research: Sachin Bobade

Tel: +91 22 40969731

E-mail: sachinb@dolatcapital.com

Associate: Nikhat Koor

Tel: +91 22 40969764

E-mail: nikhatk@dolatcapital.com

Exhibit 1: Q1FY21 Actual V/s DART Estimates

Rs mn	Actual	Estimates	Variance (%)	Comments
Revenue	29,224	39,538	(26.1)	Impact of lockdown was higher than our estimate. Decorative business volumes were down 20% in May followed by +14% in June 2020.
EBITDA	4,840	8,925	(45.8)	
EBITDA margin %	16.6	22.6	(600)	Reported employee cost was higher than our estimate due to policy change in gratuity (one off)
APAT	2,182	5,320	(59.0)	Cascading effect of lower than estimated EBITDA

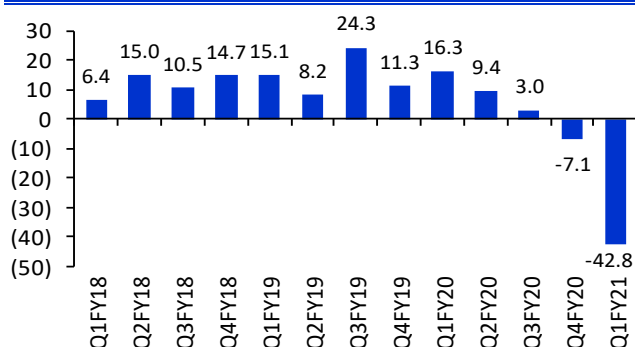
Source: Company, DART

Key concall highlights

- Decorative business achieved ~80% of base volumes in May'20 (down 20%), it was able to register volume growth of +14% YoY in June. Some pent up demand was witnessed in May'20. For overall Q1, business was able to achieve ~62% base of Q1FY20 in volume terms and 56% in value terms with upgradation and premiumization.
- Domestic decorative revenue declined 44% YoY, volume decline was lesser, with 6-8% differential between value / volume due to mix change.
- Automotive business continued to witness slowdown. In Industrial segment, both protective and powder coatings saw improvement in June. Home improvement business- Sleek and Ess Ess exhibited 50% YoY revenue decline.
- Metros constitute 40-50% of total painting demand for APL. Tier 2,3,4 cities are showing improvement with better demand conditions than metros and Tier 1. Demand in Tier 3 and 4 cities are back to pre Covid levels.
- Company has not taken any price correction in Q1FY21.
- Safe painting campaign received positive response in Q1. Royale Health Shield and Viroprotek sanitizers are also gaining traction.
- APL made judicious advertisement spends in Q1 and launched three strong campaigns.
- While RM costs softened QoQ in Q1FY20, sequential decline in gross margin was mainly due to change in mix and currency depreciation.
- Cost control measures in selling and distribution and admin expenses supported margins.
- IB posted good performance mainly as UAE and Africa were open in April and performed better than other geographies. IB witnessed double digit volume growth in June after de-growth in April and May.
- Nepal was severely affected with complete washout in April and May. Nepal opened up in June and witnessed pent up demand. It is expected to bounce back if there are no further lockdowns. Ethiopia registered low single digit growth in Q1.
- Bangladesh opened in May and performed better than Nepal. Bangladesh and Srilanka markets have mirrored India with good response in June, which should sustain if there are no further lockdowns.
- Employee expense increased significantly by 570bps to 12.4% due to policy changes regarding gratuity and increased headcount. Management clarified that it is a one-time impact and would be ~7% to sales going ahead.

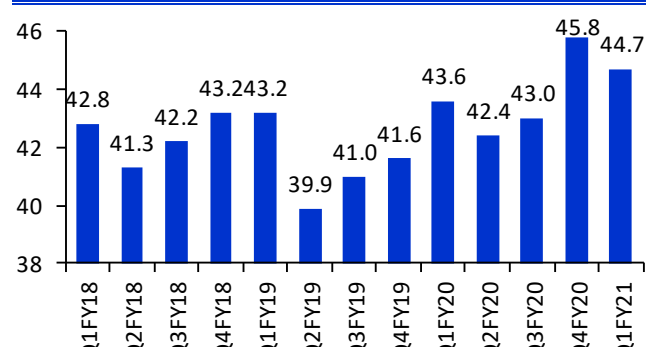
- Management has no significant capex plans for FY21E.
- Management believes that repainting and maintenance activities would gain traction as people are now spending more time at home. Also, people are spending money for waterproofing, hence this business is witnessing good response. However, discretionary spends like high end wallpaper and textures would see a setback.
- Overall waterproofing business in India is under-utilized with low per capita consumption vs China and has good potential in future. In China, waterproofing business is USD 22bn versus less than USD 1bn in India. Margins in retail waterproofing is comparable to that of paints, however institutional business margins are lower.
- Company is now back to inventory levels as of March, no exceptional piling up of inventory happening in the system, all material stocked with retailers is sold.
- There was incremental increase in incentivization/discounts to retailers in May and June to boost retailer confidence and to ensure stocking.
- Downtrading from super luxury segment in exteriors to premium and value for money segment is likely to challenge sales growth and margins going ahead.
- Company is assessing the demand scenario quarter by quarter and no planning for Diwali as of now.

Exhibit 2: Trend in Sales Growth (%)



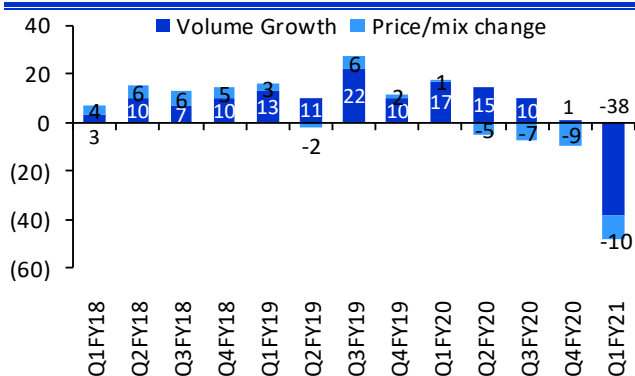
Source: DART, Company

Exhibit 3: Trend in Gross Margin (%)



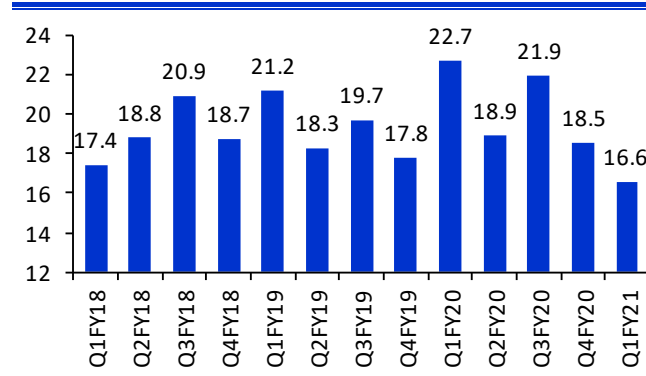
Source: DART, Company

Exhibit 4: Trend in Domestic Volume Growth (%)



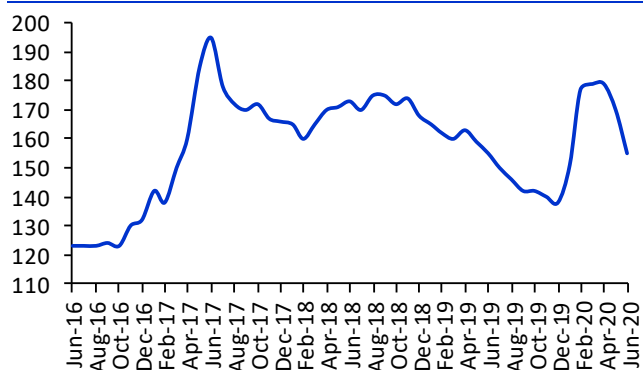
Source: DART, Company

Exhibit 5: Trend in EBITDA margins (%)



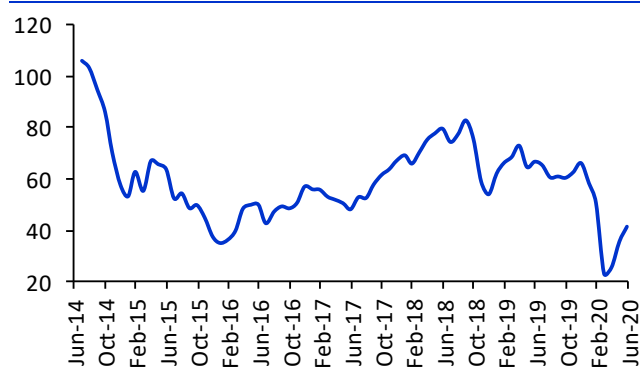
Source: DART, Company

Exhibit 6: Trend in Titanium Dioxide Price (INR/KG)



Source: DART, Company

Exhibit 7: Trend in Brent Price (USD)



Source: DART, Company

Profit and Loss Account

(Rs Mn)	FY19A	FY20A	FY21E	FY22E
Revenue	192,401	202,112	199,931	233,892
Total Expense	154,746	160,494	160,567	185,616
COGS	112,645	113,835	112,405	132,375
Employees Cost	12,368	13,662	13,904	15,539
Other expenses	29,732	32,997	34,257	37,702
EBIDTA	37,656	41,619	39,365	48,276
Depreciation	6,221	7,805	8,296	8,857
EBIT	31,434	33,814	31,069	39,419
Interest	1,053	1,023	1,062	1,177
Other Income	2,330	3,042	3,123	3,526
Exc. / E.O. items	(58)	(50)	0	0
EBT	32,654	35,783	33,130	41,769
Tax	10,981	8,549	7,604	9,493
RPAT	21,560	27,052	25,368	32,095
Minority Interest	114	183	157	181
Profit/Loss share of associates	0	0	0	0
APAT	21,618	27,101	25,368	32,095

Balance Sheet

(Rs Mn)	FY19A	FY20A	FY21E	FY22E
Sources of Funds				
Equity Capital	959	959	959	959
Minority Interest	3,631	4,030	4,187	4,368
Reserves & Surplus	93,740	100,340	110,936	124,277
Net Worth	94,699	101,299	111,895	125,236
Total Debt	6,151	3,401	3,401	3,401
Net Deferred Tax Liability	5,397	4,430	4,430	4,430
Total Capital Employed	109,877	113,160	123,913	137,435

Applications of Funds

Net Block	64,972	62,699	61,903	60,546
CWIP	2,097	1,400	1,400	1,400
Investments	13,940	15,050	15,050	15,050
Current Assets, Loans & Advances	80,006	82,240	90,225	112,112
Inventories	31,499	33,890	31,359	36,694
Receivables	19,073	17,950	16,313	18,898
Cash and Bank Balances	4,440	7,830	21,634	33,448
Loans and Advances	9,421	14,607	12,850	14,891
Other Current Assets	3,833	2,843	2,949	3,060
Less: Current Liabilities & Provisions	51,138	48,229	44,665	51,672
Payables	23,930	21,350	21,120	24,707
Other Current Liabilities	27,208	26,879	23,545	26,965
sub total				
Net Current Assets	28,869	34,012	45,560	60,440
Total Assets	109,877	113,160	123,913	137,435

E – Estimates

Important Ratios

Particulars	FY19A	FY20A	FY21E	FY22E
(A) Margins (%)				
Gross Profit Margin	41.5	43.7	43.8	43.4
EBIDTA Margin	19.6	20.6	19.7	20.6
EBIT Margin	16.3	16.7	15.5	16.9
Tax rate	33.6	23.9	23.0	22.7
Net Profit Margin	11.2	13.4	12.7	13.7
(B) As Percentage of Net Sales (%)				
COGS	58.5	56.3	56.2	56.6
Employee	6.4	6.8	7.0	6.6
Other	15.5	16.3	17.1	16.1
(C) Measure of Financial Status				
Gross Debt / Equity	0.1	0.0	0.0	0.0
Interest Coverage	29.9	33.0	29.3	33.5
Inventory days	60	61	57	57
Debtors days	36	32	30	29
Average Cost of Debt	18.3	21.4	31.2	34.6
Payable days	45	39	39	39
Working Capital days	55	61	83	94
FA T/O	3.0	3.2	3.2	3.9
(D) Measures of Investment				
AEPS (Rs)	22.5	28.3	26.4	33.5
CEPS (Rs)	29.0	36.4	35.1	42.7
DPS (Rs)	10.9	22.1	15.4	19.6
Dividend Payout (%)	48.5	78.3	58.2	58.4
BVPS (Rs)	98.7	105.6	116.7	130.6
RoANW (%)	24.1	27.6	23.8	27.1
RoACE (%)	20.2	23.1	20.2	23.3
RoAIC (%)	31.7	32.1	29.9	38.2
(E) Valuation Ratios				
CMP (Rs)	1712	1712	1712	1712
P/E	76.0	60.6	64.7	51.2
Mcap (Rs Mn)	1,642,195	1,642,195	1,642,195	1,642,195
MCap/ Sales	8.5	8.1	8.2	7.0
EV	1,632,165	1,632,646	1,618,841	1,607,027
EV/Sales	8.5	8.1	8.1	6.9
EV/EBITDA	43.3	39.2	41.1	33.3
P/BV	17.3	16.2	14.7	13.1
Dividend Yield (%)	0.6	1.3	0.9	1.1
(F) Growth Rate (%)				
Revenue	14.4	5.0	(1.1)	17.0
EBITDA	17.8	10.5	(5.4)	22.6
EBIT	10.8	7.6	(8.1)	26.9
PBT	5.6	9.6	(7.4)	26.1
APAT	9.8	25.4	(6.4)	26.5
EPS	9.8	25.4	(6.4)	26.5

Cash Flow

(Rs Mn)	FY19A	FY20A	FY21E	FY22E
CFO	25,892	27,183	37,138	39,245
CFI	(9,930)	(2,690)	(7,500)	(7,500)
CFF	(15,569)	(21,103)	(15,834)	(19,931)
FCFF	14,362	23,413	29,638	31,745
Opening Cash	4,047	4,440	7,830	21,634
Closing Cash	4,440	7,830	21,634	33,448

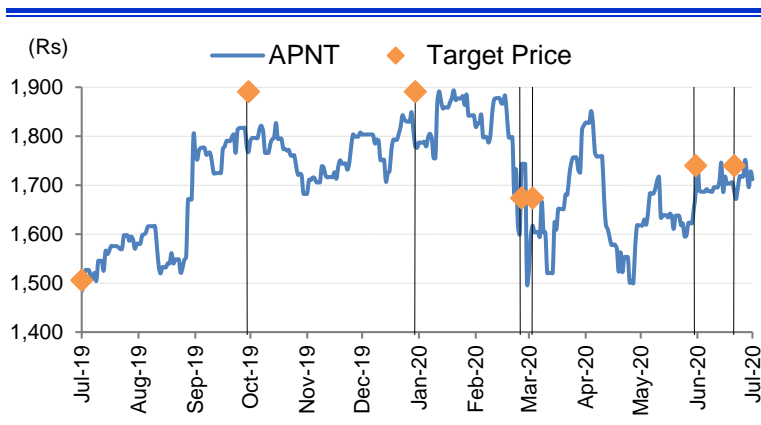
E – Estimates

DART RATING MATRIX

Total Return Expectation (12 Months)

Buy	> 20%
Accumulate	10 to 20%
Reduce	0 to 10%
Sell	< 0%

Rating and Target Price History



Month	Rating	TP (Rs.)	Price (Rs.)
Jul-19	Reduce	1,506	1,483
Oct-19	Reduce	1,891	1,767
Jan-20	Reduce	1,891	1,779
Mar-20	Reduce	1,674	1,743
Mar-20	Reduce	1,674	1,617
Jun-20	Reduce	1,740	1,684
Jul-20	Reduce	1,740	1,688

*Price as on recommendation date

DART Team

Purvag Shah	Managing Director	purvag@dolatcapital.com	+9122 4096 9747
Amit Khurana, CFA	Head of Equities	amit@dolatcapital.com	+9122 4096 9745

CONTACT DETAILS

Equity Sales	Designation	E-mail	Direct Lines
Dinesh Bajaj	VP - Equity Sales	dineshb@dolatcapital.com	+9122 4096 9709
Kapil Yadav	VP - Equity Sales	kapil@dolatcapital.com	+9122 4096 9735
Yomika Agarwal	VP - Equity Sales	yomika@dolatcapital.com	+9122 4096 9772
Jubbin Shah	VP - Derivatives Sales	jubbins@dolatcapital.com	+9122 4096 9779
Ashwani Kandoi	AVP - Equity Sales	ashwanik@dolatcapital.com	+9122 4096 9725
Lekha Nahar	AVP - Equity Sales	lekhan@dolatcapital.com	+9122 4096 9740
Equity Trading	Designation	E-mail	
P. Sridhar	SVP and Head of Sales Trading	sridhar@dolatcapital.com	+9122 4096 9728
Chandrakant Ware	VP - Sales Trading	chandrakant@dolatcapital.com	+9122 4096 9707
Shirish Thakkar	VP - Head Domestic Derivatives Sales Trading	shirisht@dolatcapital.com	+9122 4096 9702
Kartik Mehta	Asia Head Derivatives	kartikm@dolatcapital.com	+9122 4096 9715
Dinesh Mehta	Co- Head Asia Derivatives	dinesh.mehta@dolatcapital.com	+9122 4096 9765
Bhavin Mehta	VP - Derivatives Strategist	bhavinm@dolatcapital.com	+9122 4096 9705

Dolat Capital Market Private Limited.

Sunshine Tower, 28th Floor, Senapati Bapat Marg, Dadar (West), Mumbai 400013

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Registered office: Office No. 141, Centre Point, Somnath, Daman – 396 210, Daman & Diu

Board: +9122 40969700 | Fax: +9122 22651278 | Email: research@dolatcapital.com | www.dolatresearch.com
